

# HOUSE BILL REPORT

## HB 1459

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**As Reported by House Committee On:**  
Technology, Energy & Communications

**Title:** An act relating to cost-reimbursement agreements under chapter 78.52 RCW.

**Brief Description:** Authorizing oil and gas regulatory cost-reimbursements.

**Sponsors:** Representatives Kretz and B. Sullivan.

**Brief History:**

**Committee Activity:**

Technology, Energy & Communications: 2/2/07, 2/13/07 [DPS].

<p><b>Brief Summary of Substitute Bill</b></p> <ul style="list-style-type: none"><li>• Authorizes oil and gas regulatory cost-reimbursements.</li></ul>
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### HOUSE COMMITTEE ON TECHNOLOGY, ENERGY & COMMUNICATIONS

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 11 members: Representatives Morris, Chair; McCoy, Vice Chair; Crouse, Ranking Minority Member; McCune, Assistant Ranking Minority Member; Eddy, Ericksen, Hankins, Hudgins, Hurst, Takko and VanDeWege.

**Staff:** Scott Richards (786-7156).

**Background:**

Recent high prices and increased demand for oil and natural gas have renewed interest in gas exploration in Washington. Parts of the state, such as the Columbia Basin, show promise for significant reserves of natural gas.

The Department of Natural Resources (Department) regulates oil and gas exploration in Washington. The Department imposes conditions and restrictions as necessary to protect the public interest and to ensure compliance with state law, rules, and orders. The Department issues permits to drill wells and ensures compliance with applicable laws, rules, and orders. The cost of a permit is set in statute and ranges from \$250 to \$1,000 depending on the depth of the drilling. Revenues from permits go into the State General Fund.

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The Department may seek reimbursements for costs associated with pre-permitting regulatory activities, such as the preparation of environmental impact statements. But the Department lacks such authority for post-discovery activities, such as engineering analysis for reservoir size; locating and spacing of wells and operations; and reclamation and clean up of all well sites. Consequently, the Department's post-discovery regulatory activities have been funded out of the State General Fund, which were adequate when annual drilling applications numbered one or two a year.

Renewed exploration and drilling over the past year has increased. The Department reports that it is currently processing 14 applications for drilling permits, with at least five more expected before the end of the fiscal year. Three wells are actively drilling, and another five to 10 are expected to be drilled or drilling before the end of Fiscal Year 2007. Lacking the authority for post-discovery cost reimbursements, and without adequate State General Fund monies, the Department asserts it can no longer adequately regulate post-discovery drilling activities.

In 2006, the Legislature directed the Department to study and make recommendations for improving the existing legislation affecting the oil and natural gas industry. The study results were submitted to the Legislature in January 2007. Among the recommendations was one authorizing cost-reimbursement agreements for all the stages of oil and gas drilling, from exploration through production.

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## **Summary of Substitute Bill:**

### **Cost-Reimbursement Agreements**

Until July 2013, the Department may enter into a written cost-reimbursement agreement with an applicant, permit holder, or project operator to recover from the applicant, permit holder, or project operator the reasonable costs incurred by the Department in carrying out permit coordination, environmental review, application review, technical studies in support of permit processing, or orders issued by the oil and gas supervisor and permit compliance.

The cost-reimbursement agreement must identify the specific tasks, costs, and schedule for work to be conducted under the agreement. Applicants must request cost-reimbursement agreements.

### **Third-Party Contracting**

The Department must use funds required by the agreements to contract with third-parties to carry out the work specified in the cost-reimbursement agreement and to recover the Department's administrative costs. The state ethics laws apply to the agreements and to persons hired as a result of the agreements.

Allowable administrative costs are those costs incurred by the Department in receiving an application for a drilling permit, establishment of a development unit, or approval or issuance of a pooling order including negotiating the cost-reimbursement agreement, negotiating the contracts for services with third parties, management of the cost-reimbursement and services

contracts, reviewing the reports of the third party, and issuing the permits, orders, or agreements.

The Department shall charge \$40 per hour to recover administrative costs of the contract for services with the third-party. The Legislature may review and adjust the per hour rate if there is a significant increase in departmental employee wages.

The Department must review and oversee the work performed by the third-party. Final decisions that involve policy matters must be made by the Department and not by the third-party consultant.

**Interim Measure**

Cost-reimbursement agreements are considered an interim measure until oil and gas development activities necessitate additional Department staffing resources.

**Substitute Bill Compared to Original Bill:**

The substitute provides a termination date of July 1, 2013, for which the Department of Natural Resources may enter into written cost-reimbursement agreements.

Departmental activities that are considered administrative in managing third-party work related to written cost-reimbursement agreements are specified.

The substitute establishes a departmental charge of \$40 per hour to recover administrative costs of the contract for services with the third-party. The Legislature may review and adjust the per hour rate if there is a significant increase in departmental employee wages.

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**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date of Substitute Bill:** The bill takes effect 90 days after adjournment of session in which bill is passed.

**Staff Summary of Public Testimony:**

(In support) In 2006, the Legislature authorized the Department of Natural Resources (Department) to study and make recommendations on oil and gas drilling in the state. This bill relates to one of the key recommendations. The Department is now permitted to recover expenses through cost-reimbursements agreements for the oil or gas exploration phase but not for the development phase if there is a discovery of oil or gas.

In case of a discovery of oil or gas, the Department would need to deal with offset wells, development units, and pooling agreements. These activities should be allowable through current cost-reimbursement agreement statute and is a logical extension of the work the Department performs during the exploration phase. However, the state Attorney General's Office says that current state statute does not allow for cost-reimbursement agreements to be

applied after the exploration phase. This bill seeks to allow for cost-reimbursement agreements to be used during the post discovery phase.

(Opposed) None.

**Persons Testifying:** Representative Kretz, prime sponsor; and Ron Teissere, Department of Natural Resources.

**Persons Signed In To Testify But Not Testifying:** None.